In the Supreme Court of the United States.

OCTOBER TERM, 1918.

ALVAH CROCKER ET AL., TRUSTEES, petitioners,
v.
JOHN F. MALLEY, COLLECTOR OF INTERNAL REVENUE.
No. 649.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIRST CIRCUIT

BRIEF FOR THE UNITED STATES.

STATEMENT OF CASE.

This case arises under the income-tax act of 1913 (38 Stat., c. 16, p. 166). It involves the taxes for which the petitioners were liable on a gross income for the years 1913, 1914, and 1915 of $604,077.66, $580,098.03, and $762,916.23, respectively. (Rec., pp. 16, 18, and 19.)

They were assessed, as an association, under subsection G (a) of the act (38 Stat., p. 172), which levies a tax upon the net income of "every corporation, joint stock company or association, and every insurance company, organized in the United States, no matter how created or organized, not including

partnerships," and paid, under protest, $10,875.40, which amount this suit was brought to recover.

They claim that they are not an association and therefore not taxable as such, but should have been assessed and taxed only as fiduciaries under subsection D of the act (38 Stat., p. 168).

In either event the rate of taxation is the same, but in the case of fiduciaries there is deducted from the gross income, in order to arrive at the net income, all dividends received from corporations which had themselves paid the tax, while in the case of associations no such deduction is allowed.

RESULT BELOW.

The District Court sustained the contention of the plaintiffs and allowed a recovery for the amount paid less $1,321.33 for which they would have been liable if assessed as beneficiaries, and rendered judgment for $9,554.07, with interest from October 11, 1916. (Rec., pp. 33–35.)

The Circuit Court of Appeals sustained the contention of the Government, reversed the judgment, and remanded the case with directions to enter judgment in favor of the defendant. (250 Fed. Rep., 817, 825.)

QUESTION INVOLVED.

The question is whether the plaintiffs must return this income and pay tax on it in their own behalf, as an association, or whether they are mere fiduciaries who must make return and pay the tax on behalf of the persons for whom they act.

THE FACTS.

The history of the property or estate from which the income in question was derived is as follows: For many years prior to the year 1912, Crocker, Burbank & Co., Inc., was a corporation organized under the laws of the State of Maine, but with its only place of business and its assets situated in Massachusetts. It had been organized for the purpose of incorporating the business of Crocker, Burbank & Co., a partnership which had for many years done business as paper manufacturers in Massachusetts. In 1912 the stockholders of the Maine corporation were eight of the members of the families of the former partners of this firm.

In 1912 a new corporation was organized under the laws of Massachusetts with the name of Crocker, Burbank & Company, Inc., and with a capitalization of $2,400,000.00.

The original partnership and the Maine corporation had a number of mills along the banks of the Nashua River, and, in order to control the possible pollution of the stream, had acquired numerous and considerable outlying tracts of land not otherwise pertaining to their business.

When the new company was formed it did not desire to acquire the ownership of the real estate of the old corporation except certain of the mill properties and the water power. It accordingly took over seven mill properties in fee and, pending the development of further plans, took from the

Maine corporation a lease of its remaining real estate, including one mill property then in process of construction, the outlying parcels of real estate and some tenements occupied by employees, and issued in consideration for the transfer all its capital stock to the Maine corporation.

It was then decided to dissolve the Maine corporation. To accomplish this, that corporation conveyed to the Massachusetts corporation the seven mill properties and took the shares of capital stock of the latter corporation in payment. It then conveyed the remaining real estate, subject to the lease to the Massachusetts corporation, to Alvah Crocker and four others of its eight stockholders and turned over to the same parties the stock of the Massachusetts corporation which it had received. These five parties then executed on March 29, 1912, what they termed a "declaration," setting out the terms and conditions upon which they would hold the property turned over to them. By this paper they declared that "we will, and our heirs and successors shall, hold said granted premises, and all other funds and property at any time transferred to and received by the trustees hereunder for the purposes, with the powers, and subject to the provisions hereof, for the benefit of the cestui que trusts (who shall be trust beneficiaries only, without partnership, associate or any other relation whatever inter sese), and upon the trusts following."

TERMS OF THE TRUST.

The purposes, powers, and provisions of the trust were declared to be:

1. To convert the property into money and distribute the net proceeds among those owning beneficial interests therein, as evidenced by the receipt certificates issued by the trustees, it being understood, however, and agreed "that the trustees may, in their uncontrolled discretion, defer or postpone such conversion and distribution, except that the same shall not be postponed beyond the end of 20 years from and after the death of the last survivor of" certain named persons, and that until conversion the interests of the cestui que trusts shall be considered as personal property.

2. Until conversion and distribution, the trustees were to have for the purpose of managing and controlling the property and for all purposes of sale, lease, mortgage, exchange, improvement, and development, and any and all arrangements, contracts, and dispositions of the trust property, or any part thereof, "all and as full discretionary powers and authority as they would have if they were themselves the sole and absolute beneficial owners thereof in fee simple."

3. That the trustees were to collect and receive all rents and income from the property, and semiannually, or oftener at their convenience, "to distribute such portion thereof as they may, in their discretion, determine to be fairly distributable net income, to and among the several cestui que trusts" according to their

respective interests, but were to have "full authority from time to time to use any funds on hand, whether received as capital or income, for purposes of any repair, improvement, protection, or development of the property held hereunder, or the acquisition of other property as the trustees may determine to be wise and expedient, for the protection and development of the trust property as a whole pending its conversion and distribution."

4. The trust was declared in favor of and for the benefit of the eight shareholders of the Maine corporation and the trustees were to "issue proper receipt certificates," which were to be transferable and to conclusively evidence the ownership of respective interests in the trust, and the trustees, from time to time, on request, were to issue new certificates upon surrender of the old to evidence any new or subdivided interests.

5. The trustees were to have authority to borrow money and give any pledge, mortgage, or other security which they should deem wise, and no lender was ever to have any liability to see to the application of the funds loaned.

6. The trustees were to have authority to employ such agents and attorneys as they might think proper, and were not to be personally responsible for any misconduct, errors, or omissions of such agents or attorneys, if employed and retained with reasonable care.

7. The trustees were to keep proper books of accounts and records "of their proceedings and doings,"

and at least annually render an account to any beneficiary requesting same, but no trustee was to give bond or have any liability except for the results of his own gross negligence or bad faith.

8. The recording of the trust instrument was to be at such times and places as the trustees should determine necessary or expedient.

9. The trustees were to have full power at any time, pending the termination of the trust, to transfer the whole or any part of the property then held by them to any corporation which they might acquire or cause to be organized for the more convenient or expedient holding or management of the property, taking any securities issued by such corporation in exchange therefor, with authority to become directors or officers of any such corporation.

10. The compensation of the trustees for their services was not to exceed a total of 1 per cent of the gross income received by them, "unless, at any time, a majority in interest of the cestui que trusts consent in writing to some larger compensation for any past service."

11. Any trustee was to have the right to resign, and the method of filling vacancies was as follows: "Any vacancy in the office of the trustee, however occasioned, shall be filled by the remaining trustees by an instrument in writing, signed by them and assented to in writing by the holder or holders of a majority in amount of the beneficial interests herein, such appointment to be in like manner attached to the original of this instrument or recorded" at the

place at which the original trust declaration was recorded.

12. In the event of the absence or incapacity of any of the trustees, the remaining trustees, being a majority of the whole, were authorized to exercise all of the powers of the trust.

13. It was provided that "the terms and provisions of this trust may be modified at any time or times by an instrument in writing, signed, sealed, and acknowledged by the then trustees, assented to in writing by a majority in interest of the cestui que trusts, and attached to the original of this instrument or recorded" where the original trust declaration was recorded.

14. The certificate in writing of the trustees as to any resignation or appointment of trustees and as to any modification of the trust was to be conclusive evidence in favor of all persons dealing in good faith with the trustees in reliance upon such certificate.

15. It was provided that "the title of this trust (fixed for convenience) shall be 'The Wachusett Realty Trust,' and the term 'Trustees' in this instrument shall be deemed to include the original and all successor trustees."

16. Unless earlier terminated, the trust was to terminate and the property to be distributed at the end of 20 years after the death of the last survivor of Charles T. Crocker, Samuel E. M. Crocker, and Alvah Crocker, and of the lawful issue of any of them living at the time of the execution of the trust.

It will be observed that the purposes and objects of the trust are fully stated and the powers conferred upon the trustees fully defined. Within the scope of these purposes and objects, the powers conferred are plenary. But the certificate holders do not surrender all control. The right is reserved to them to have a voice in filling vacancies in the office of trustee, in determining whether the nature and scope of the enterprise shall be changed, and in fixing the compensation, in excess of 1 per cent, to be received by the trustees, which right is to be exercised by the concurring action of a majority in interest. During the short period since the trust was organized no occasion has arisen for the exercise of this right, but it has existed and still exists.

During the years for which the taxes in question were collected, the trustees managed and controlled the property in accord with the provisions of the trust. They collected the income, which consisted of rentals, dividends declared by the Massachusetts corporation, and a small amount of interest, which, less charges, disbursements, and taxes or similar expenses, they distributed among the certificate holders.

The present receipt certificate holders are 14 members of the Crocker families, two connections by marriage of that family, and one unrelated friend of the family.

BRIEF.

(I.)

The income-tax law requires every person, corporation, joint-stock company, or association, except partnerships, to make returns and pay taxes on his or its own behalf on all income accruing to him or it. The same parties must return all income which accrues to other parties but passes through their hands and, on this, they must pay the taxes, on behalf of those to whom the income goes. (38 Stat., c. 16, p. 166.)

(II.)

Trusts for the management and control of business or property are very common in Massachusetts, though uncommon elsewhere. Their legal status depends upon their terms. They may, of course, be such that the trustees are mere fiduciaries. The Massachusetts courts have held that they may be partnerships. The Federal court sitting in Massachusetts has held that they are sometimes unincorporated companies or associations. *Williams* v. *Milton*, 215 Mass., 1; *In re Associated Trust*, 222 Fed. Rep., 1012.

(III.)

To be within the income-tax law an association is not required to be one organized under statutory authority. (36 Stat., c. 6, pp. 11, 112; *Eliot* v. *Freeman*, 220 U. S., 179; 38 Stat., c. 16, p. 166; Bouvier's Law Dictionary, vol. 1, p. 269; 4 Cyc., p. 301; Words and Phrases, vol. 1, p. 584.

(IV.)

Under the terms of the declaration of trust and the authorities above cited, the Wachusett Trust is an association within the meaning of the income-tax law.

ARGUMENT.

The Circuit Court of Appeals held that the income in question had not arisen or accrued to the beneficiaries of the trust as individuals, but had accrued to the group or body of individuals who were organized under the trust so as to be an association within the meaning of the Income Tax Act. An examination of the act, it is confidently insisted, fully justifies this conclusion.

RETURNS REQUIRED BY THE ACT.

A large amount of income has been received and it is conceded that the Wachusett Realty Trust must, under the law, make a return of the same for purposes of taxation. The act provides for four kinds of returns: (1) Returns of income to be made by individuals; (2) returns by corporations, joint stock companies, and associations, "no matter how created or organized"; (3) returns by fiduciaries, which may be individuals, corporations, or associations; (4) withholding returns, which may be made by individuals, corporations, associations, or partnerships. It will be observed that returns of the first two kinds are to include only the income accruing to the party making the returns and on which such party must pay the tax on its or his own behalf. The

remaining two kinds are returns which must include incomes accruing to other parties but passing through the hands of the party making the return, which latter party is required to pay the tax on behalf of the party to whom the income ultimately goes.

The question then is whether the income collected by the Wachusett Trust and distributed to its certificate holders accrued to it or to the certificate holders individually. It may well be that a corporation or association may be required to make returns of both kinds. Thus, a trust company may act as guardian or executor, and in that capacity may receive the income from the trust property and out of the same may receive compensation for its services. In making its own return as a corporation or association, the compensation which it thus receives is a part of the income accruing to it and must be included in the return. The portion of the income, however, which it pays to its ward or holds for the estate which it is administering would not be included in this report, because it is income accruing to the beneficiaries. The corporation or association, however, has received it in a fiduciary capacity, and the law requires that the tax on it shall be paid before it is passed on to the beneficiary, and for this reason the corporation or association must make a report in its capacity as a fiduciary and must withhold from the income which has accrued to the beneficiary the tax and pay the same to the Government.

It will also be seen that the returns upon which the party making them must pay taxes on his or its own behalf embrace (1) income accruing severally to individuals and (2) income accruing collectively to bodies or groups of individuals associated in corporations, joint stock companies, or associations.

STATUS OF WACHUSETT REALTY TRUST.

It thus becomes necessary to determine just what the trust in question is. Is it an organization for the management and control of property for the common benefit of the equitable owners? Does the income collected by it accrue to it as an organized group or body? Or is it a mere fiduciary for the collection and transmission of income accruing to individuals?

This case arose in Massachusetts, where such trusts, varying much as to details, are very common, though unusual elsewhere. They are resorted to as a method by which property owned by a number of people in common is not infrequently managed and controlled for the common benefit. They are not creatures of statute like a corporation or like joint stock companies authorized by statutes in some of the States, but not in Massachusetts.

Counsel have argued that this trust is not a partnership. Thus far, there is no quarrel. The Government has taxed this income under a section of the act which excludes partnerships from its operation. But counsel have cited Massachusetts cases holding that similar trusts are not partnerships and urge

them as authority for the contention that the trustees are mere fiduciaries. (*Williams* v. *Milton*, 215 Mass. 1, and other cases.) An examination of these cases, however, will show that the court was only called on to determine whether a particular trust was a partnership or merely some form of trust not amounting to a partnership. If not a partnership, the question as to just what it was did not arise. The main significance of these cases, as they bear on this case, is that they establish the rule that trusts in this general form may be and often are a form of business organizations. Counsel have a long list of cases in which they were held to be partnerships. Upon the same principle, they may, of course, be also voluntary business associations. The courts of that State, however, apparently have had no occasion to determine whether any particular trust was or was not an *association*. Under the tax laws, the property of a *partnership* is assessed for taxation at the place where it is located. On the other hand, in the case of a *trust* which is not also a partnership and in which the interests of the different beneficiaries are represented by certificates, as in this case, the certificates are taxable at the residence of the owners, if within the State, and the aggregate amount of assessments thus made on the certificates is deducted from the assessment made against the trust at its domicile. This latter rule applies to all such trusts, except those which are held to be partnerships.

In determining these tax questions, then, the only question before the court in each case was, whether

the trust in question was a partnership or some other kind of trust. In the cases cited in brief of counsel in which it was held not to be a partnership, the holding simply was that it was a trust as distinguished from a partnership. There was, of course, no holding beyond this as to what kind of a trust it was. In other words, for all that was held, it might be either a trust in which the trustee merely acted in a fiduciary capacity or it may have been a trust so organized as to amount to a business corporation. This is the view which has been taken of these cases by the Federal courts sitting in Massachusetts. In *In re Associated Trust* (222 Fed. Rep., 1012) the court dealt with a trust very similar to the one now under consideration and was called on to determine whether it was "an unincorporated company" within the meaning of the bankruptcy act. The court, referring to the Massachusetts cases, held that that particular trust was not a partnership. It held, however, that this did not preclude the trust from being some other kind of business association. On the contrary, it held that the trust under consideration was an unincorporated company, which is only another name for an association, within the meaning of the bankruptcy act.

The contention of the Government is that the Wachusett Realty Trust is neither a partnership nor a corporation, but some sort of business organization which lies between the two and partakes to some extent of the nature of both. As stated above, and as held in the case just referred to, there is nothing

in the Massachusetts cases which precludes such an association or unincorporated company from being organized by a declaration of trust. The real question is, whether the terms of this particular trust have the effect of organizing a business association. Such associations may vary largely as to detail. There is no fixed rule of law specifying all their features. In each case it is for the court to determine the purpose and intent of the parties and the legal effect of the instrument declaring the trust.

ASSOCIATION NOT REQUIRED TO BE CREATED UNDER STATUTORY AUTHORITY.

The corporation-tax law of 1909 (36 Stat., c. 6, pp. 11, 112) undertook to levy an excise tax upon corporations and joint-stock associations. But that act was expressly limited to such corporations or joint-stock associations as were "organized under the laws of the United States" or of any State of the United States. And in *Eliot* v. *Freeman* (220 U. S., p. 178), decided in 1911, this court held that the tax applied only to associations which were organized under some statutory authority, quoting with approval from Cook on Corporations the following:

> There is an essential difference between a joint-stock company as it exists at common law and a joint-stock company having extensive statutory powers conferred upon it by the State within which it is organized. The latter kind of joint-stock company is found in England and in the State of New York. To such an extent have these statutory powers been conferred on joint-stock

> companies that the only substantial difference between them and corporations is that the members are not exempt from liability as partners for the debts of the company. (P. 186.)

Subsequent to this decision, when Congress came to pass the income-tax act of 1913 it avoided using the language which this court had held to exclude purely voluntary associations and instead used the language "organized in the United States, no matter how created or organized." There was thus clearly evinced a purpose to make the act broader than the act of 1909 and to include business associations which could not be said to have been organized under or by virtue of the laws of any State or Government. It can not be doubted, then, that there are voluntary associations which Congress intended to tax. The question is, what is an association within the meaning of this act. Bouvier's Law Dictionary defines the word "association" as follows (vol. 1, p. 269):

> In the United States this term is used to signify a body of persons united without a charter but upon the methods and forms used by incorporated bodies for the prosecution of some enterprise.

And again:

> An unincorporated company is fundamentally a large partnership, from which it differs mainly in the following particulars: That it is not bound by the acts of the individual partners, but only by those of its managers; that shares in it are transferable; and that it is not dissolved by the retirement, death, bankruptcy, etc., of its individual members.

And in Cyc., vol. 4, p. 301, it is said:

> An association may be defined to be a body of persons acting together, without a charter, but upon the methods and forms used by incorporated bodies, for the prosecution of some common enterprise.

In Words and Phrases, vol. 1, p. 584, it is said:

> Association is "confederacy or union for particular purpose, good or ill." This term is used throughout the United States to signify a body of persons united without a charter, but upon the methods and forms used by incorporated bodies, for the prosecution of some common enterprise.

WACHUSETT REALTY TRUST A BUSINESS ASSOCIATION.

The definitions quoted are of necessity general in their character. It is perhaps impossible to frame a definition which will accurately cover every case in which the legal effect of what is done is to form an association. It will doubtless be conceded that any form of an unincorporated company is an association within the meaning of this act. Clearly, that is the very kind of organization which it was intended to tax, and probably no better description of an unincorporated company can be given than the one found in the case of *In re Associated Trust, supra*, as follows:

> The words "unincorporated company" are not found in any Massachusetts statute which has been considered in connection with these organizations. Their meaning in the Bankruptcy Act is by no means certain. The word

> "unincorporated" is clear; the word "company" in this connection is much less definite. It would seem to imply an association of individuals, not partners, carrying on business under a distinct name, and having common rights inter se, but having no individual ownership in the joint property, no individual control over the business in which their joint capital is embarked, and no direct individual liability for the company's debts. Its use in connection with the word "unincorporated" would seem to imply that the organization should have some of the attributes usually found in corporations.

More accurate language to describe the Wachusett Trust could scarcely be used, provided it can be fairly said that that organization has "some of the attributes usually found in corporations." In the case cited, the court found that the trust then before it had the following features which were similar to those usually found in corporations, namely: (1) That it had a capital contributed by the certificate holders; (2) that future managers were to be chosen by the certificate holders; (3) that the character, scope, and size of the enterprise might be changed by the certificate holders and might be terminated by them; (4) that these rights were given to the certificate holders in the instrument by which the Associated Trust was constituted.

The Wachusett Trust has all of these features, with one slight modification. The certificate holders may not, independent of the trustees, choose future

managers or change the scope of the enterprise or terminate it. They are not, however, entirely divested of control in this respect. The trustees can do these things only with the written assent of a majority in interest of certificate holders. In other words, these things can not be done without the consent of a majority in interest of certificate holders. In effect, there is reserved to them a veto power as to these matters. In short, in many matters only those stockholders who are also trustees have a voice. As to the matters in which they have a voice, their power is limited to permitting action to be taken by giving their consent or preventing action by withholding consent. But this, in principle, is similar to a feature frequently found in corporate organizations. In a corporation it is not essential that all stockholders shall have the same power of control, or even that all shall have a voice in the management. Thus, preferred stock may be issued, and, very generally, the holders of such stock are not entitled to vote in corporate meetings. So, in this organization the original voting power was vested in the five stockholders who were named as trustees. The organization would not have been dissimilar to that of a corporation if this power had been unlimited. As to certain matters it was unlimited, these being matters which the original parties in interest agreed should be committed to the judgment of the trustees. But as to matters

which involved a change of the original scheme or plan all certificate holders were given a voice by requiring that such things could not be done without the consent of a majority in interest of them. For the same reason, therefore, that the trust involved in *In re Associated Trust, supra,* was held to have some of the attributes usually found in corporations, and to be therefore an unincorporated company, the trust now involved is likewise an unincorporated company or association. Other points of similarity between this trust and a corporation are that both do business under a distinct name; that the managers of both are not personally liable for misconduct, errors, or omissions of their agents, if employed and retained with reasonable care, but only for the results of their own gross negligence or bad faith; and that, in those matters as to which the shareholders are empowered to act, the action of a majority, not in numbers but in interest, binds all.

It is true the declaration of trust says the shareholders "shall be trust beneficiaries only, without partnership, associate, or any other relation whatever *inter sese.*" Citation of authorities, however, can not be necessary to show that this statement can have no effect if the result of what was actually done was to constitute the legal relation of partners or any other kind of associates.

A recital of the history of this trust and the purposes of its promoters will clearly show that it

is a business organization which properly comes within the meaning of the word "association" as used in the act in question.

Eight persons were the equitable owners of property which had theretofore been managed and controlled through the instrumentality of a corporation. It was not desired to continue this corporation longer. At the same time, it was not deemed expedient to at once sell the property and distribute the proceeds or to divide it in kind. The parties did not desire to enter into a partnership. They did not all care to participate in the active management and control of the property. Pending the time when it could be advantageously converted into money and distributed, it was desired that it should be kept together, managed, controlled, developed, and perhaps added to by new purchases. The object of the trust was to accomplish these purposes. Since neither a corporation nor a partnership was desired, some other organization was necessary. The plan adopted was to have the property conveyed to five of their number, who should assume its management, control, and development for the common benefit. When this conveyance was made, these five then held the title to the property in which the other three had an equitable interest. The five, therefore, in pursuance of the arrangement entered into by all, immediately executed a declaration of trust, which served the double purpose of fixing the respective rights of the equitable owners and furnishing what was not

dissimilar to a charter, under which they were to manage and control the property for the benefit of all. That the parties understood that they were forming an organization which, in its general nature, was at least similar to a corporation is evidenced from the fact that one of the powers which it was agreed the trustees should exercise was the power to transfer all the property to a corporation if it should be found best to organize such a corporation for the more convenient or expedient holding or management of the property. It was also anticipated that before the termination of the trust it might be found necessary to fill vacancies in the office of trustees or to modify the terms of the trust instrument; but in both of these matters it was provided that all parties in interest should have a voice—that is, these things should not be done unless assented to in writing by a majority in interest of the certificate holders.

If a corporation had been organized, the interest of each stockholder would have been evidenced by the issue of a stock certificate. Under the organization as it was formed, each party in interest received a certificate showing what his interest was. The stock certificate would have been transferable. The certificates of interest in this case were likewise transferable. In this case the holders of certificates, who were also trustees, had a larger voice in the management of the organization than those who were not trustees. There were thus two classes of interested parties. In the same way there are fre-

quently two classes of stockholders in a corporation, one of which has only a limited voting power or no such power at all. The fact that the declaration of trust fixes a time in the future when the trust must terminate does not make the organization dissimilar to a common form of corporate organization. It is not uncommon for corporate charters, notably in the case of national banks and many corporations created in the early days by special acts of legislatures, to be granted for only a limited period of time. This organization certainly has most of the characteristics of joint stock companies as authorized by statutes of many of the States, of which this court said in *Eliot* v. *Freeman, supra*, "that the only substantial difference between them and corporations is that the members are not exempt from liability as partners for the debts of the company." And it may be said that this trust, while not quite so much like a corporation in some respects as these joint stock companies, approaches somewhat nearer to a corporation in that, through the device of conveying property so that it is to be managed by trustees, individual liability of the partners for the debts of the organization is perhaps escaped. We have here a body of persons united without a charter, but upon methods and forms similar in many respects to incorporated bodies for the prosecution of a business enterprise. The organization is not bound by the acts of the individuals interested in it, but only by the trustees to whom the management is committed. Shares in it are transferable; it is not dissolved

by the retirement, death, or bankruptcy of any of the individuals composing it, and these, it is respectfully submitted, include all the essentials of a business association within the meaning of the income tax law.

Another consideration which would seem to be controlling is this: As we have seen, a person or corporation making the return required of a fiduciary reports income which has not accrued to it, but which has accrued to another who is liable for the tax. In other words, in order to be a mere fiduciary the rights of the beneficiary must be fixed so that he is entitled to the income collected and so that his right to same does not depend upon the will of a corporation or other organization as to whether it shall be distributed or shall be retained as the property of the organization collecting it. In this case, the declaration of trust does not require the distribution of any particular part of the income. In fact, the trustees, as the managers of the organization, are empowered to withhold all of the income and use it for the development of the trust property itself. Thus, it is expressly provided that the trustees shall only "distribute such portion thereof as they may, in their discretion, determine to be fairly distributable net income." And what is meant by this is clearly shown by the further provision that they shall have "full authority from time to time to use any funds on hand, whether received as capital or income, for purposes of any repair, improvement, protection, or development of the property held hereunder, or the acquisi-

tion of other property as the trustees may determine to be wise and expedient, for the protection and development of the trust property as a whole pending its conversion and distribution." It is difficult to see how language could have been employed which would make it plainer that the right of the certificate holders to a distribution of any of the income should be absolutely in the control of the trustees. The result is that when any income is received, the trustees themselves decide whether it shall be distributed among the certificate holders or shall be retained and used for the benefit of the trust property. In effect, it is treated just like the remainder of the trust—that is, the trustees may at any time make a partial distribution or they may retain the whole until the termination of the trust. In other words, they have the same power that a corporation has to determine whether profits realized shall be distributed among stockholders or added to the surplus of the corporation. In either case, no income accrues to the certificate holder or stockholder until the organization having control of the business determines whether there shall be a distribution. It follows, therefore, when the Wachusett Trust collected income from the trust property that income accrued to the business organization operating under that name and remained its income until it saw fit to distribute it. While in its hands it was its income and not income of the individual certificate holders. There would seem, therefore, no escape from the conclusion

reached by the Circuit Court of Appeals that the income sought to be taxed was the income of a business association and subject to taxation as such.

It is respectfully submitted that the judgment of the Circuit Court of Appeals should be affirmed.

WILLIAM L. FRIERSON,
Assistant Attorney General.

FEBRUARY, 1919.

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SUPREME COURT OF THE UNITED STATES

No. 649.—October Term, 1918.

Alvah Crocker et al., Trustees, Petitioners, *vs.* John F. Malley, Collector of Internal Revenue.	On Writ of Certiorari to the United States Circuit Court of Appeals for the First Circuit.

[March 17, 1919.]

Mr. Justice Holmes delivered the opinion of the Court.

This is an action to recover taxes paid under protest to the Collector of Internal Revenue by the petitioners, the plaintiffs. The taxes were assessed to the plaintiffs as a joint-stock association within the meaning of the Income Tax Act of October 3, 1913, c. 16, Section II, G, (a), 38 Stat. 114, 166, 172, and were levied in respect of dividends received from a corporation that itself was taxable upon its net income. The plaintiffs say that they were not an association but simply trustees, and subject only to the duties imposed upon fiduciaries by Section II, D. The Circuit Court of Appeals decided that the plaintiffs, together, it would seem, with those for whose benefit they held the property, were an association, and ordered judgment for the defendant, reversing the judgment of the District Court. 250 Fed. Rep. 817.

The facts are these. A Maine paper manufacturing corporation with eight shareholders had its mills on the Nashua River in Massachusetts and owned outlying land to protect the river from pollution. In 1912 a corporation was formed in Massachusetts. The Maine corporation conveyed to it seven mills and let to it an eighth that was in process of construction, together with the outlying lands and tenements, on a long lease, receiving the stock of the Massachusetts corporation in return. The Maine corporation then transferred to the plaintiffs as trustees the fee of the property subject to lease, left the Massachusetts stock in their hands, and was dissolved. By the declaration of trust the plaintiffs declared that they held the real estate and all other property at any time received by them thereunder, subject to the provisions thereof, 'for the benefit of the *cestui que trusts* (who shall be trust bene-

ficiaries only, without partnership, associate or other relation whatever *inter sese*)' upon trust to convert the same into money and distribute the net proceeds to the persons then holding the trustees' receipt certificates—the time of distribution being left to the discretion of the trustees, but not to be postponed beyond the end of twenty years after the death of specified persons then living. In the meantime the trustees were to have the powers of owners. They were to distribute what they determined to be fairly distributable net income according to the interests of the *cestui que trusts* but could apply any funds in their hands for the repair or development of the property held by them, or the acquisition of other property, pending conversion and distribution. The trust was explained to be because of the determination of the Maine corporation to dissolve without waiting for the final cash sale of its real estate and was declared to be for the benefit of the eight shareholders of the Maine Company who were to receive certificates subject to transfer and subdivision. Then followed a more detailed statement of the power of the trustees and provision for their compensation, not exceeding one per cent. of the gross income unless with the written consent of a majority in interest of the *cestui que trusts*. A similar consent was required for the filling of a vacancy among the trustees, and for a modification of the terms of the trust. In no other matter had the beneficiaries any control. The title of the trust was fixed for convenience as The Massachusetts Realty Trust.

The declaration of trust on its face is an ordinary real estate trust of the kind familiar in Massachusetts, unless in the particular that the trustees' receipt provides that the holder has no interest in any specific property and that it purports only to declare the holder entitled to a certain fraction of the net proceeds of the property when converted into cash 'and meantime to income'. The only property expressly mentioned is the real estate not transferred to the Massachusetts corporation. Although the trustees in fact have held the stock of that corporation and have collected dividends upon it, their doing so is not contemplated in terms by the instrument. It does not appear very clearly that the eight Maine shareholders might not have demanded it had they been so minded. The function of the trustees is not to manage the mills but simply to collect the rents and income of such property as may be in their hands, with a large discretion in the application of it, but with a recognition that the receipt holders are entitled to it

subject to the exercise of the powers confided to the trustees. In fact, the whole income, less taxes and similar expenses, has been paid over in due proportion to the holders of the receipts.

There can be little doubt that in Massachusetts this arrangement would be held to create a trust and nothing more. 'The certificate holders . . . are in no way associated together nor is there any provision in the [instrument] for any meeting to be held by them. The only act which (under the [declaration of] trust) they can do is to consent to an alteration . . . of the trust' and to the other matters that we have mentioned. They are confined to giving or withholding assent, and the giving or withholding it 'is not to be had in a meeting but is to be given by them individually'. 'The sole right of the *cestuis que trust* is to have the property administered in their interest by the trustees, who are the masters, to receive income while the trust lasts, and their share of the corpus when the trust comes to an end'. *Williams* v. *Milton*, 215 Mass. 1, 10, 11; *ibid.* 8. The question is whether a different view is required by the terms of the present act. As by D. above referred to trustees and associations acting in a fiduciary capacity have the exemption that individual stockholders have from taxation upon dividends of a corporation that itself pays an income tax, and as the plaintiffs undeniably are trustees, if they are to be subjected to a double liability the language of the statute must make the intention clear. *Gould* v. *Gould*, 245 U. S. 151, 153. *United States* v. *Isham*, 17 Wall. 496, 504.

The requirement of G. (a) is that the normal tax thereinbefore imposed upon individuals shall be paid upon the entire net income accruing from all sources during the preceding year "to every corporation, joint-stock company or association, and every insurance company, organized in the United States, no matter how created or organized, not including partnerships." The trust that has been described would not fall under any familiar conception of a joint-stock association, whether formed under a statute or not. *Smith* v. *Anderson*, 15 Ch. D. 247, 273, 274, 277, 282. *Eliot* v. *Freeman*, 220 U. S. 178, 186. If we assume that the words 'no matter how created or organized' apply to 'association' and not only to 'insurance company', still it would be a wide departure from normal usage to call the beneficiaries here a joint-stock association when they are admitted not to be partners in any sense, and when they have no joint action or interest and no control over the fund.

On the other hand the trustees by themselves cannot be a joint-stock association within the meaning of the act unless all trustees with discretionary powers are such, and the special provision for trustees in D. is to be made meaningless. We perceive no ground for grouping the two—beneficiaries and trustees—together, in order to turn them into an association, by uniting their contrasted functions and powers, although they are in no proper sense associated. It seems to be an unnatural perversion of a well-known institution of the law.

We do not see either that the result is affected by any technical analysis of the individual receipt holder's rights in the income received by the trustees. The description most in accord with what has been the practice would be that, as the receipts declare, the holders, until distribution of the capital, were entitled to the income of the fund subject to an unexercised power in the trustees in their reasonable discretion to divert it to the improvement of the capital. But even if it were said that the receipt holders were not entitled to the income as such until they got it, we do not discern how that would turn them into a joint-stock company. Moreover the receipt holders did get it and the question is what portion it was the duty of the trustees to withhold.

We presume that the taxation of corporations and joint-stock companies upon dividends of corporations that themselves pay the income tax was for the purpose of discouraging combinations of the kind now in disfavor, by which a corporation holds controlling interests in other corporations which in their turn may control others, and so on, and in this way concentrates a power that is disapproved. There is nothing of that sort here. Upon the whole case we are of opinion that the statute fails to show a clear intent to subject the dividends on the Massachusetts corporation's stock to the extra tax imposed by G. (a).

Our view upon the main question opens a second one upon which the Circuit Court of Appeals did not have to pass. The District Court while it found for the plaintiffs, ruled that the defendant was entitled to retain out of the sum received by him the amount of the tax that they should have paid as trustees. To this the plaintiffs took a cross writ of error to the Circuit Court of Appeals. There can be no question that although the plaintiffs escape the larger liability, there was probable cause for the defendant's act. The Commissioner of Internal Revenue rejected the plaintiff's claim, and the statute does not leave the matter clear. The

recovery therefore will be from the United States. Rev. Sts. § 989. The plaintiffs, as they themselves alleged in their claim, were the persons taxed, whether they were called an association or trustees. They were taxed too much. If the United States retains from the amount received by it the amount that it should have received, it cannot recover that sum in a subsequent suit.

Judgment of the Circuit Court of Appeals reversed.

Judgment of the District Court Affirmed.

A true copy.

Test:

Clerk Supreme Court, U. S.